

#2488

signed 11-3-99

**IN THE UNITED STATES BANKRUPTCY COURT
FOR THE DISTRICT OF KANSAS**

In re:

**HUDSON OIL COMPANY, INC.,
HUDSON REFINING COMPANY, INC.,
HUDSON VAN OIL COMPANY OF
KANSAS CITY, INC.,
HUDSON REALTY COMPANY, INC.,
HUDSON STATIONS, INC.,
HUDSON VAN OIL COMPANY OF
FLORIDA, INC.,
HUDSON OIL COMPANY OF
CALIFORNIA, INC.,
HUDSON VAN OIL COMPANY,

DEBTORS.**

**CASE NO. 84-20002
CASE NO. 84-20003
CASE NO. 84-20004

CASE NO. 84-20005
CASE NO. 84-20006
CASE NO. 84-20007

CASE NO. 84-20008

CASE NO. 84-20009
CHAPTER 11**

**ORDER GRANTING MOTION FOR DISTRIBUTION OF FUNDS
TO THE SECRETARY OF THE U.S. DEPARTMENT OF LABOR**

This matter is before the court on the joint motion of the Secretary of the United States Department of Labor (“DOL”) and the post-confirmation Unsecured Creditors Committee (“the Committee”) for an order requiring certain money to be distributed as provided in the joint liquidating plan that was confirmed in these bankruptcy cases. Interested parties Salman Maneck and Merrill Lynch Pierce Fenner & Smith (“Merrill Lynch”) object to the motion. The DOL appears by Janice Miller Karlin, an Assistant United States Attorney for the District of Kansas. The Committee appears by counsel Thomas Mullinix of Evans & Mullinix, P.A. Mr. Maneck appears by counsel Benny J. Harding. Merrill Lynch appears by counsel Gregory S. Gerstner of Seigfreid, Bingham, Levy, Selzer & Gee. The Court has reviewed the relevant materials and heard argument, and is now ready to rule.

FACTS

The relevant facts are not disputed. A joint liquidating chapter 11 plan was confirmed in these

bankruptcy cases in September 1990. The plan established the Hudson Oil Liquidating Trust (“the Trust”), naming Walter Kellogg as trustee (“the Trustee”); his main obligation was to liquidate the assets of the bankruptcy estates and distribute the proceeds according to the plan. The plan also designated \$2,200,000 in cash to be the “Unsecured Creditor Fund (“UCF”), and provided that the Trustee was to receive the UCF and hold it separate from any other money or property. The plan provided the UCF could only be used for certain specified purposes. Some of the UCF was to be distributed to general unsecured creditors shortly after the plan was confirmed. Another portion, \$440,000, was to be held in a segregated fund pending the completion of sales of certain assets, and to be distributed to either the DOL or the unsecured creditors according to a formula based on the amount produced by the sales. The DOL’s claim to the money was based on a prepetition judgment that it had obtained against one or more of the debtors for the benefit of their underpaid employees.

The sales of the assets took some time to accomplish, and while they were being pursued, certain other relevant events took place. For a time after confirmation, the \$440,000 was held in a bank account under the control of Mr. Mullinix and another person. The reason for this arrangement has not been disclosed, but its existence has no effect on the Court’s decision. At some point, in order to comply with a request from the United States Trustee and to obtain a better return, most of the money was invested through an account with Merrill Lynch and the rest was deposited with Union Bank. The Union Bank account is not involved in the present dispute. The Merrill Lynch account was established in the Trust’s name and a portion of the UCF was transferred into the account so the Trustee would have control of it as called for by the plan. The Trustee has always maintained the UCF in segregated accounts and not commingled it with any other money under his control. Ultimately, the amount of the proceeds from the sales of the assets was so small that the DOL became entitled under

the plan's formula to all \$440,000.

During the liquidation process, Mr. Maneck agreed to buy certain real estate from the Trust, depositing \$20,000 with the Trustee, probably as earnest money. Later, Mr. Maneck canceled the contract and demanded the return of his deposit, but the Trustee refused. Mr. Maneck sued the Trust for breach of contract and conversion. Early in 1999, Mr. Maneck obtained a judgment for the \$20,000 plus prejudgment interest of \$3,150 and punitive damages of \$30,000.

On June 17, 1999, Mr. Maneck garnished the Trust's account at Merrill Lynch. Merrill Lynch answered the garnishment, stating that there was sufficient money in the account to pay the judgment. On July 30, the state court issued an order for Merrill Lynch to pay Mr. Maneck the amount of the judgment and release the balance of the account to the Trust. Apparently, Merrill Lynch has not yet complied with this order, and Mr. Maneck may have asked the state court to grant him judgment against Merrill Lynch based on its failure to pay him.

On August 16, the DOL and the Committee filed their joint motion before this Court for an order directing Merrill Lynch and Union Bank to pay the UCF over to the DOL, as called for in the plan. Mr. Maneck and Merrill Lynch have now appeared before this Court by filing objections to the joint motion. All these parties appeared for a hearing on September 29, and the Court took the matter under advisement.

DISCUSSION AND CONCLUSIONS

The question before the Court is whether the fact the UCF had been placed in the Merrill Lynch account in the Trust's name and under the Trustee's control allowed Mr. Maneck's garnishment to take priority over the DOL's right to the money. The answer is no. Mr. Maneck does not question that the UCF was generated by the debtors' business operations before their chapter 11 plan was

confirmed. He does not challenge the assertion that the plan called for the UCF to be held solely for the benefit of either the DOL or the general unsecured creditors, depending on the outcome of the sales of the specified assets. He does not challenge the assertion that the Merrill Lynch account contained a portion of the UCF, together with interest or income it earned, and never contained any other assets. By the time of Mr. Maneck's garnishment, the sales had been completed and the DOL had become entitled to all the money in the account.

Mr. Maneck contends that he is an innocent judgment creditor who had no knowledge that the account he garnished might have belonged to anyone other than the Trust, and the DOL and unsecured creditors simply failed to protect the UCF from his claims when they turned the money over to the Trustee. Kansas courts have made clear, however, that a garnishment can reach only the judgment debtor's interest in the garnished property. *Purma v. Stark*, 224 Kan. 642, 644-45 (1978); *Turner v. Williams*, 114 Kan. 769, 772-73 (1923). The fact the garnishing judgment creditor had no knowledge that another party owned the property does not alter this rule. *Nelson v. Boula*, 207 Kan. 771, 774 (1971); *Chatterton v. Clayton*, 150 Kan. 525, 527 (1939); *Hall v. Kansas City Terra Cotta Co.*, 97 Kan. 103, 105-06 (1916). Although title to the UCF was in the Trust's name, the plan made clear that the Trust held bare legal title and all the beneficial interest in the UCF actually belonged to either the DOL or the general unsecured creditors. Subsequent events determined that it all belonged to the DOL. Under Kansas law, Mr. Maneck's garnishment could not affect the ownership of the UCF.

Both Mr. Maneck and Merrill Lynch suggest that Merrill Lynch could be required to pay the balance in the Trust's account twice if this Court orders it to pay the money to the DOL. Certainly this would be an unjust result. Under Kansas law, the DOL and the Committee could have intervened in

the garnishment proceeding to assert the DOL's ownership of the money in the account. *Dailey v. Walden*, 7 Kan. App. 2d 712, 715-16 (1982). Although they instead filed a motion before this Court, Mr. Maneck's appearance here has brought all relevant parties before one court so their dispute can be completely resolved, effectively achieving the same result as intervention in the state court would have. Since Mr. Maneck has appeared before this Court to oppose the joint motion of the DOL and the Committee, the Court can avoid the potential injustice to Merrill Lynch of conflicting rulings by directing Mr. Maneck to dismiss the garnishment proceeding.

For these reasons, Mr. Maneck is hereby directed: (1) to inform the state court that this Court has determined that the funds belong to the DOL; (2) to ask the state court to vacate its order directing Merrill Lynch to pay him, and (3) to ask the court to dismiss the garnishment proceeding. Assuming the state court grants these requests, Merrill Lynch should then disburse to the DOL the funds it holds in the account in the Trust's name. Upon paying the funds to the DOL, Merrill Lynch will be released from any further liability to Mr. Maneck, the DOL, or the Committee because of the account that held the UCF. If the state court will not grant the requests, the parties should inform this Court of the state court's ruling and their positions about further action this Court should take.

IT IS SO ORDERED.

Dated at Topeka, Kansas, this _____ day of November, 1999.

JAMES A. PUSATERI
CHIEF BANKRUPTCY JUDGE